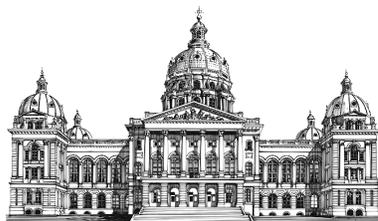

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State Capitol
Des Moines, IA 50319
January 30, 2007

Individual Development Accounts

ISSUE

This *Issue Review* examines how Individual Development Accounts (IDAs) operate and perform in selected states.

AFFECTED AGENCIES

Department of Economic Development (DED)
Department of Workforce Development (IWD)
Community Colleges
Department of Education
Department of Human Services (DHS)

CODE AUTHORITY

Chapter 541A, Code of Iowa
Chapter 20, Code of Federal Regulations, Sections 663.400, 663.410, 663.420, 663.430, 663.510 and 663.585 (Workforce Investment Act (WIA) Programs).

BACKGROUND

Individual Development Accounts (IDAs) are matched savings accounts that can typically be used only for purchasing a first home, capitalizing a small business, or for educational or job training expenses to enable low-income families to save, build assets, enter the financial mainstream, and develop financial independence. Accounts are held at local financial institutions. Contributions by lower income participants are matched using both private and public sources. Provisions for IDAs have been in federal law since 1998. Since then, legislation to expand the use of IDAs, as well as newer forms of matched savings accounts (e.g., KIDS Accounts) has been considered by Congress.

The match incentive, similar to an employer match for 401(k) contributions, is provided through a variety of government and private sector sources. Organizations that operate IDA programs often couple the match incentive with financial literacy education, training to purchase an asset, and case management. The following describes how a participant moves through a typical IDA program:

STEP 1 - Orientation sessions provide participants with information about the program, asset-building options, importance of savings, and the lifetime development of assets.

STEP 2 - Participants meet with staff to develop a savings plan, discuss income and consumer patterns. Participants attend mandatory training on banking, investing, and money management.

STEP 3 - Participants open IDA savings accounts with cooperating financial partners (bank or credit union). Participants sign a contract expressing a commitment to save. The program tracks how much participants save, how much they receive in matching funds, and accumulated interest.

STEP 4 - Participants, with staff assistance, make bank withdrawals from savings. Participants can use funds to purchase a home, continue education, or start a business and continue to save for the future.

CURRENT SITUATION

Building on the 13 Federal American Dream Policy Demonstration sites across the nation, hundreds of IDA programs have emerged. The Corporation for Enterprise Development (CFED) estimates there is between 500 and 1,000 IDA programs nationwide with at least 20,000 individuals participating in IDAs or having completed IDA programs. Since these programs have developed as a decentralized grassroots movement, complete data is not available. Currently, IDA programs serve some of the hardest-to-reach groups, such as the low-income and those eligible for Temporary Assistance for Needy Families (TANF).

The *Assets 2005, Number 1*, newsletter, published by the CFED, reported the following results of a national survey of organizations that offer IDAs. The account holders are primarily female (66.0%). The following tables provide some of the findings about account holders.

| Annual Income | Percentage | Age | Percentage |
|----------------------|-------------------|-------------|-------------------|
| \$0 - \$10,000 | 9.0% | 0 - 12 | <1% |
| \$10,000 - \$20,000 | 38.0% | 13 - 18 | 3.0% |
| \$20,000 - \$30,000 | 35.0% | 19 - 29 | 30.0% |
| \$30,000 - \$40,000 | 16.0% | 30 - 49 | 56.0% |
| \$40,000 - \$50,000 | 2.0% | 50 and Over | 11.0% |
| \$50,000 and Over | <1% | | |

Federal Assets for Independence Act (AFIA) grants fund more IDA programs than any other reported source of government or private funding. Organizations may have multiple funding sources. A list of funding sources and the percentage of the respondents using that funding source is provided in the table below.

| Funding Source | Percentage |
|------------------------|-------------------|
| AFIA | 65.2% |
| Foundations | 45.4% |
| Financial Institutions | 41.3% |
| CDBG | 19.8% |
| Individuals | 19.1% |
| Employers | 17.7% |

Most responding IDA programs allow program funds to be used for the first-time purchase of a home. Funding for small business start-up and expansion is the second most common permissible

use and post-secondary education is third. The table below provides the percentage of IDA organizations that permit an IDA to be used for the listed use.

| Permissible Uses | Percentage |
|---------------------------------------|------------|
| First-time Home Purchase | 94.0% |
| Small Business Start-up and Expansion | 75.0% |
| Post-secondary Education | 74.0% |
| Vocational Training | 48.0% |
| Computer Purchase | 33.0% |
| Home Repair | 20.0% |
| Automobile Purchase | 19.0% |
| Manufactured Home Purchase | 19.0% |
| Subsequent Home Purchase | 13.0% |
| Other | 8.0% |
| Land Purchase | 6.0% |
| Enrichment Activities | 5.0% |
| First and Last Month's Rent | 5.0% |
| Childcare | 4.0% |
| Retirement | 2.0% |
| Medical Expenses | 2.0% |

Twenty-eight percent of American Dream Demonstration (ADD) Program "graduates" bought a home, 23.0% started or expanded their own business, and 21.0% pursued higher education. The rest used savings for home repair, job training, or retirement.

The match rate varies from organization to organization and depends upon the permissible use and funding source for the match. Workforce Investment Act (WIA) funding can also be used for training through an IDA.

Cost-Effectiveness – The Center for Social Development reported the cost of providing one month of IDA services, excluding matches, for a participant was approximately \$64 at the Community Action Program of Tulsa County, between October 1998 and June 2001. The average administrative cost for each dollar deposited, excluding matching funds, into an account was \$2.20.

Iowa IDA Program

The Iowa IDA Program was passed by the 1993 General Assembly in SF 268 (Iowa Investment Program Act). The legislation supports the use of IDAs for the following:

- (1) Educational costs at an accredited institution of higher education.
- (2) Training costs for an accredited or licensed training program.
- (3) Purchase of a primary residence.
- (4) Capitalization of a small business start-up.
- (5) An improvement to a primary residence which increases the tax basis of the property.
- (6) Emergency medical costs for the account holder or for a member of the account holder's family, however, a withdrawal for this purpose is limited to once during the life of the account and the amount of the withdrawal must not exceed 10.0% of the account balance at the time of the withdrawal.

Chapter 541A, Code of Iowa, establishes the DHS as the Program Administrator for an Iowa IDA Program. However, the Department has reallocated Temporary Assistance for Needy Families (TANF) funds to other programs and the Program is no longer operated. The Department had used the Program to support first-time homeownership for the low-income.

Iowa currently has one organization, the Institute for Social and Economic Development, which supports IDAs, as established by Chapter 541A, Code of Iowa, and one of the permissible uses is education. The organization uses AFIA grant funding to match a participant's investment, for a stated goal, of up to \$2,000 over a six-month period.

Other States

Connecticut

To date, the Connecticut Legislature has appropriated \$1.2 million for the IDA Program. The Program has leveraged federal funds in excess of \$900,000, as well as over \$1.0 million in contributions from financial institution partners and other businesses, foundations, United Ways, and municipalities. The Connecticut Department of Labor oversees the Program and four federally-funded Assets for Independence IDA Programs, providing the opportunity for over 550 low- and moderate-income families to become asset owners. During the 2006 Session, the Legislature passed a Bill establishing a Connecticut Housing Trust Fund, and stipulated that each year \$300,000 from the Fund be used for housing IDAs.

Michigan

The Michigan IDA Program matches savings, including funds received from Earned Income Tax Credits (EITCs), to help families accumulate more money to invest in a home, education, job training, or a small business. A family must apply to participate in the Program through one of more than 50 organizations that currently offer the Program for over 1,400 active accountholders. The basic requirements are income-related, less than 200.0% of the federal poverty level, completion of an economic literacy course, training related to an investment goal, and saving money toward the goal. Once completed, savings of up to \$1,000 are matched at a ratio of 3:1 for a home purchase and 2:1 for post-secondary education, job training, or to start or expand a small business.

The State of Michigan contracted with ISED Solutions to complete an independent evaluation report, through year three (September 2000 - September 2003) of the Project. The evaluation found the typical IDA participant is a 33-year-old single African-American woman with some college education, a full-time job, a monthly household income of about \$1,700 (\$20,000 annually), and two children living at home.

Nearly 80.0% of all participants plan to purchase a home, 10.0% intend to start a business, and 8.0% plan to use it for education. Regular savings by participants increased from 25.0% to 71.0%, with 87.0% percent reporting they expect to save regularly in the future. Additional findings of the study are as follows:

- 99.0% have been affected positively by being in their IDA Program and 84.0% believe the financial management education classes have helped them save.
- 90.0% are more aware of their credit rating. Families showed, on average, a 12.0% to 23.0% increase in their credit score depending on the credit score source.
- 83.0% report they are more likely to work or stay employed since opening their IDA.
- After entering an IDA Program, the percentage of households receiving government assistance decreased from 29.0% to 6.0%.

- Through September 29, 2006, 909 IDA Participants had made an asset investment (625 homes purchased, 165 education account uses, and 119 business account uses). The mortgages leveraged to date exceed \$55.0 million.
- The Program has leveraged \$3.0 million in private sector funding, \$4.0 million from the State (including DHS and Michigan State Housing Development Authority funds), and \$2.0 million in Federal Assets for Independence Act funding. All five Regional Coordinating Organizations have received AFIA support to be used by the participating organizations.

North Carolina

According to the year-end statistics for 2005, the North Carolina Department of Labor (NCDOL) IDA Program consists of 29 sites that serve 50 counties. This is up from 27 sites and 44 counties in 2004. The Program currently has 1,084 account holders, an increase of 756 compared to 2004. The Program has had 312 participants graduate in homeownership, micro-enterprise, or postsecondary education. The graduates purchased 255 homes, started 31 businesses, and made 26 educational investments. As of December 2005, IDA participants saved an aggregate of \$1.0 million, acquired more than \$610,000 in matching grant funds, and purchased an estimated \$21.5 million in assets. The NCDOL completed the first year of its Assets for Independence Act (AFIA) grant this year, with a 94.0% success rate and a total of 187 graduates. In addition, the North Carolina Department of Health and Human Services contracted with the NCDOL to administer \$180,000 in Temporary Assistance for Needy Families (TANF) funds for IDAs.

ALTERNATIVES

- Since the IDA Program enacted in Iowa is not being operated at this time, the General Assembly could consider reviewing the topic.
- A direct appropriation could be made to postsecondary educational institutions that could be used for tuition assistance for individuals that demonstrate need. For example, Kirkwood Community College Continuing Education and Training Services have proposed a Gap Training and Skills Development Program for targeted populations. The Program would develop and implement a continuing education non-credit certificate tuition program. The target population would be individuals interested in non-credit certification in the areas of advanced manufacturing, information technologies, and healthcare fields. Individuals earning up to 80.0% of the area median family income would be eligible to receive tuition assistance.
- State workforce boards could partner with IDA organizations and maximize services available through Workforce Investment Act funding.
- In other states, some IDA training programs are a partnership between an employer and a nonprofit organization that administers the program for the employer. These partnerships could be encouraged. The requisite financial education is taught in most part by the nonprofit partners and employers allow the financial education to be provided at the worksite during the employees' normal work hours and without loss of pay. Matching funds for the IDAs are provided by a number of sources, including endowments, financial institutions, federal agencies, or the employer.

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